

**DEPARTMENT OF STATE REVENUE
LETTER OF FINDINGS NUMBER: 98-0781
FINANCIAL INSTITUTIONS TAX
For Years 1992, 1993, 1994, 1995, AND 1996**

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ISSUES

I. Financial Institutions Tax – Nexus

Authority: IC § 6-5.5-3-1; IC § 6-5.5-3-4

Taxpayer protests the inclusion of interest income earned from loans to Indiana customers.

II. Financial Institutions Tax – Calculation of Adjusted Gross Income

Authority: IC § 6-5.5-1-10; IC § 6-5.5-2-1; IC § 6-5.5-2-3; IC § 6-5.5-4-2

Taxpayer protests the inclusion of loss amounts derived from transactions such as capital losses, partnership losses, and loan losses in taxpayer's adjusted gross income.

STATEMENT OF FACTS

Taxpayer is a regional bank holding company. Taxpayer files a consolidated federal return with approximately 70 banking subsidiaries, only two of its subsidiaries have filed corporate returns in Indiana. The banking subsidiaries are engaged in general retail and corporate banking as well as lease financing, discount brokerage, investment advisory services, and insurance agencies.

I. Financial Institutions Tax – Nexus

DISCUSSION

The audit added income from seven of taxpayer's out of state entities that received income from loans to Indiana customers. The seven entities are located in the Pacific

Northwest and do not have a location in the state of Indiana. The inclusion of the income and the taxpayer's protest were both based on IC § 6-5.5-3-1, which states in relevant part:

For the purposes of this article, a taxpayer is transacting business within Indiana in a taxable year only if the taxpayer:

....

(3) regularly sells products or services of any kind or nature to customers in Indiana that receive the product or service in Indiana;

(4) regularly solicits business from potential customers in Indiana;

(5) regularly performs services outside Indiana that are consumed within Indiana;

(6) regularly engages in transactions with customers in Indiana that involve intangible property, including loans but not property described in section 8(5) of this chapter, and result in receipts flowing to the taxpayer from within Indiana;....

....

(8) regularly solicits and receives deposits from customers in Indiana.

Taxpayer protests that the entities at issue did not solicit business in Indiana and, "More likely than not, Indiana customers of the above entities were not solicited as residents of Indiana. It appears then that the above entities would not have been regularly soliciting business in Indiana according to Indiana Statute Section 6-5.5-3-1 during the audit years." Taxpayer protest letter of 12/4/98, page 1.

The inclusion of interest income is based on the auditor's finding that the taxpayer's activities within the state did rise to the level contemplated by IC § 6-5.5-3-1. IC § 6-5.5-3-4 defines "regularly solicit business" as:

A person is presumed, subject to rebuttal, to regularly solicit business within Indiana if:

(1) the person conducts activities described in section 1(3), 1(5), and 1(6) of this chapter with twenty(20) or more customers within

Indiana during the taxable year; or

(2) the sum of the person's assets, including the assets arising from loan transactions, and the absolute value of the person's deposits attributable to Indiana equal at least five million dollars (\$5,000,000).

The assessment against the entities was based on the number of Indiana customers at each entity. While taxpayer presents an explanation that may account for the Indiana activity, taxpayer's explanation is unsupported by evidence and does not rebut the statutory presumption of "regularly solicit business." Taxpayer entities receive receipts from over twenty Indiana residents as defined in IC § 6-5.5-3-4(1) and the receipts are from loans as required by IC § 6-5.5-3-1(6).

FINDINGS

The taxpayer's appeal is denied.

II. Financial Institutions Tax – Calculation of Adjusted Gross Income

Taxpayer protests the inclusion of loss amounts derived from transactions such as capital losses, partnership losses, and loan losses in taxpayer's adjusted gross income. In support of this protest, taxpayer cites the Indiana code definition of sales income and the general definition of gross receipts and maintains that they do not include any modification by loss amounts.

The franchise tax is not on Indiana sales or gross receipts; rather IC § 6-5.5-2-1 (a) establishes:

There is imposed on each taxpayer a franchise tax measured by the taxpayer's adjusted gross income or apportioned income for the privilege of exercising its franchise or the corporate privilege of transacting the business of a financial institution in Indiana...

While IC § 6-5.5-2-1 establishes the tax, IC § 6-5.5-2-3 establishes the calculation to be followed by this taxpayer:

For a nonresident taxpayer that is not filing a combined return the taxpayer's apportioned income consists of the taxpayer's adjusted gross income for that year multiplied by the quotient of:

- (1) the taxpayer's total receipts attributable to transacting business in Indiana, as determined under IC 6-5.5-4- 4;
divided by
- (2) the taxpayer's total receipts from transacting business in all taxing jurisdictions, as determined under IC 6-5.5-4.

This statute explicitly requires reference to IC § 6-5.5-4, with the calculation in question being further defined in IC § 6-5.5-4-2, which states in relevant part:

For purposes of computing receipts or the receipts factor under this article the following apply:

- (1) "Receipts" means gross income (as defined in IC 6-5.5-1-10), plus the gross income excluded under Section 103 of the Internal Revenue Code, less gross income derived from sources outside the United States. However, upon the disposition of assets such as securities and money market transactions, when derived from transactions and

activities in the regular course of the taxpayer's trade or business, receipts are limited to the gain (as defined in Section 1001 of the Internal Revenue Code) that is recognized upon the disposition.

(2)

IC § 6-5.5-1-10, as referenced above, serves to define "Gross Income" for purposes of this section as:

"Gross Income" means gross income (as defined in Section 61 of the Internal Revenue Code) for federal income tax purposes.

Taxpayer protested the inclusion of three categories of losses in the denominator of the apportionment formula. Section 61 of the IRS code requires these losses to be included in gross income calculations for all three categories. However, IC § 6-5.5-4-2(1) does explicitly note "receipts are limited to the gain" for receipts generated by "disposition of assets such as securities and money market transactions." Consequently, taxpayer protest to the inclusion of capital losses from the disposition of assets such as securities and money market transactions is sustained, the protest is denied for the remaining categories, including capital losses from transactions involving property.

FINDINGS

The taxpayer's appeal is sustained as to capital losses from the sale of securities and money market transactions, denied as to all other losses.